13.

Office Supreme Court, U. S.
FILED
MAR 19 1917
JAMES D. MAHER
CLERK

No. 9[redacted]148

Supreme Court of the United States

GRATIOT COUNTY STATE BANK,
A Corporation, Petitioner.

vs.

D. LLOYD JOHNSON,
As Trustee of the St. Louis Chemical Company, Bankrupt, Respondent.

SUPPLEMENTAL BRIEF IN BEHALF OF RESPONDENT.

EDWARD J. MOINET,
EDWIN H. LYON,
WILLIAM A. BAHLKE,
Attorneys for Respondent.

FRANK R. GIBSON, PRINTER, 510 10TH STREET

SUPREME COURT OF THE UNITED STATES

GRATIOT COUNTY STATE BANK,
A Corporation, Petitioner.

vs.

D. LLOYD JOHNSON,
As Trustee of the St. Louis Chemical Company, Bankrupt, *Respondent.*

SUPPLEMENTAL BRIEF IN BEHALF OF RESPONDENT.

When the original brief of Respondent was prepared herein, counsel did not have before them the amendment to the Judicial Code, which is entitled in part "further to define the jurisdiction" of the Supreme Court, (Public, No. 258, 64th Congress, approved, September 6, 1916). Neither did counsel know of its existence.

Section 237 of the Judicial Code as thereby amended repealed the right to review in this Court by writ of error a final judgment or decree in any suit in the highest Court of a State in which a decision in the suit could be had, "where any title, right, privilege, or immunity is claimed under the Constitution, or any treaty or statute of, or commission held or authority exercised under the United States, and the decision is against the title, right, privilege or im-

munity especially set up or claimed, by either party, under such Constitution, treaty, statute, commission, or authority * * *."

The amendment, however, adds the provision, that "it shall be competent for the Supreme Court, by certiorari or otherwise, to require that there be certified to it for review and determination with the same power and authority and with like effect as if brought up by writ of error, any cause * * *, where any title, right, privilege, or immunity is claimed under the Constitution, or any treaty or statute of, or commission held or authority exercised under the United States, and the "decision is either in favor of or against the title, right, privilege, or immunity especially set up or claimed, by either party, under such Constitution, treaty, statute, commission, or authority."

The section as amended by the Act of 1916, governs or controls the application of the petitioner herein, since said act took effect thirty days after its approval or October sixth, 1916. It was therefore in effect before the judgment of the Michigan Supreme Court was entered, which date was December 21st, 1916, (p. 372).

The 1916 amendment to Section 237 of the Judicial Code, restricted or abridged the right of review by writ of error in this court by the elimination of the provision first quoted; it broadened or conferred the power on this court on "certiorari or otherwise" to require that there be certified to it for review and determination, any cause wherein a final judgment or decree has been rendered or passed by the highest court of a State in which a decision could be had in certain cases specified, which includes cases of the character or description arising under federal statutes and as set forth in the petition of the petitioner in the instant application.

The purpose of the amendment of September 6, 1916,

was evidently to prevent the abuses which arose by dilatory and vexatious applications to this court by raising imaginary or possible federal questions under the provision thus stricken from Section 237 of the Judicial Code, without depriving this court of jurisdiction to review in meritorious cases by "certiorari or otherwise," judgments of the highest courts of the States, where is drawn in question as is sought in this case, any "title, right, privilege or immunity" claimed under any statute of the United States, "and the decision is either in favor of or against the title, right, privilege or immunity especially set up or claimed, by either party" under such statute.

We understand that where appeals are allowed by "certiorari or otherwise" under the second paragraph or subdivision of Section 237 as amended, and certified to this court for review, the allowance of the appeal is not a matter of right to review the decision of the State court, even though a federal question is involved, but is discretionary and to be granted only in extraordinary cases that may arise.

The two questions raised by petitioner in its application for writ of certiorari herein, arise, only, if at all, as rights claimed under a statute of the United States and may be faily states as follows:

The first assignment reaches the question of the competency of testimony in the trial court.

The second assignment raises the question of whether there was any evidence in the trial court to take the case to the jury upon the question: Did the defendant have reasonable cause to believe, that a preference was intended by the bankrupt in its making the voidable preferential payments in question?

We respectfully submit that such questions are not re-

viewable or within contemplation of the statute since the amendment approved September 6, 1916.

This application is clearly within the evils sought to be remedied by said amendment. To permit a review in this Court upon such questions under the present statute, would make applications to the Court for review by "certiorari or otherwise," under the second paragraph of Section 237 as thus amended, equally as common and often as frivolous and pretentious as applications for writ of error under Section 237 before its recent amendment. Nothing will have been accomplished by the amendment of 1916, if applications such as that of the petitioner in this case, may be granted.

Respectfully submitted,

EDWARD J. MOINET,
EDWIN H. LYON,
St. John's, Mich.
WILLIAM A. BAHLKE,
Alma, Mich.
Attorneys for Respondent.

GRATIOT COUNTY STATE BANK *v.* JOHNSON, AS TRUSTEE OF THE ST. LOUIS CHEMICAL COMPANY, BANKRUPT.

CERTIORARI TO THE SUPREME COURT OF THE STATE OF MICHIGAN.

No. 148. Submitted January 20, 1919.—Decided March 17, 1919.

Although an adjudication of bankruptcy concludes all the world as to the status of the debtor *qua* bankrupt, it does not bind strangers as to the facts or subsidiary questions of law upon which it is based. P. 248.

In a suit by the trustee to recover, as illegal preferences, payments made by the bankrupt, within four months before the filing of the

involuntary petition, to a creditor who did not appear in the bankruptcy proceedings, the adjudication of bankruptcy is not conclusive evidence of the bankrupt's insolvency when such payments were made, even if based upon allegations and findings that the bankrupt was insolvent throughout the four months and that, during that period, he gave illegal preferences to such creditor, among others. *Id.*

Sections 18*b* and 59*f* of the Bankruptcy Act, allowing creditors to intervene, are permissive only; and, unless a creditor exercises the right, he remains a stranger to the proceedings. P. 249.

The purpose of Congress in expressly authorizing such interventions in involuntary bankruptcy proceedings was to guard against improvident adjudications and protect those creditors whose peculiar interests might be prejudiced by establishing the status of bankruptcy. P. 250.

193 Michigan, 452, reversed.

THE case is stated in the opinion.

Mr. Elliott G. Stevenson and *Mr. William L. Carpenter* for petitioner.

Mr. Edward J. Moinet and *Mr. William A. Bahlke* for respondent. *Mr. Edwin H. Lyon* was on the briefs.

MR. JUSTICE BRANDEIS delivered the opinion of the court.

The trustee in bankruptcy of the St. Louis Chemical Company brought suit in a state court of Michigan against the Gratiot County State Bank to recover, as illegal preferences, payments made to it within four months before the filing of the involuntary petition. The Bank denied the allegation that the Chemical Company was insolvent when the payments were made. To establish that fact, the Trustee offered in evidence the adjudication together with the petition on which it was based and the special master's report which it confirmed. The latter found

that the debtor had been insolvent for four months or more before the filing of the petition and had made, while so insolvent, certain preferences. The Bank was not actually a party to the bankruptcy proceedings and had taken no part therein. The trial court held that this evidence was not only admissible but established conclusively that the debtor was insolvent throughout the four months; and it entered judgment for the Trustee which was affirmed by the Supreme Court of Michigan (193 Michigan, 452). The case comes here on writ of certiorari (243 U. S. 645). The only question presented is whether the state courts erred in holding that the record of the adjudication made the fact of insolvency at the time of the payments *res judicata* as against the Bank.

First. The Trustee contends that adjudication in bankruptcy, being in the nature of a judgment *in rem*, establishes not only the status of the debtor as a bankrupt, but also the essential findings of fact on which that judgment was based. The adjudication is, for the purpose of administering the debtor's property, that is, in its legislative effect, conclusive upon all the world. Compare *Shawhan* v. *Wherritt*, 7 How. 627, 643. So far as it declares the status of the debtor, even strangers to the decree may not attack it collaterally. *Michaels* v. *Post*, 21 Wall. 398, 428; *New Lamp Chimney Co.* v. *Ansonia Brass & Copper Co.*, 91 U. S. 656, 661–662. Compare *Hebert* v. *Crawford*, 228 U. S. 204, 208–209. But an adjudication in bankruptcy, like other judgments *in rem*, is not *res judicata* as to the facts or as to the subsidiary questions of law on which it is based, except as between parties to the proceeding or privies thereto. *Manson* v. *Williams*, 213 U. S. 453, 455.[1] This court applied the

[1] See also *In re Henry Ulfelder Clothing Co.*, 98 Fed. Rep. 409, 413–414; *In re Schick*, 2 Ben. 5, Fed. Cas. No. 12,455; *Silvey & Co.* v. *Tift*, 123 Ga. 804; *Durant* v. *Abendroth*, 97 N. Y. 132; *Lewis* v. *Sloan*, 68 N. C. 557, 562–563.

principle in *Wood* v. *Davis*, 7 Cranch, 271, where a judgment that a mulatto woman was born free was held, as between strangers, not conclusive that her children were free. The rule finds abundant illustration in cases dealing with decedents' estates, *Tilt* v. *Kelsey*, 207 U. S. 43, 52; *Brigham* v. *Fayerweather*, 140 Massachusetts, 411; and in cases involving the marriage status, *Luke* v. *Hill*, 137 Georgia, 159; *Burlen* v. *Shannon*, 3 Gray, 387; *Wilson* v. *Mitchell*, 48 Colorado, 454, 469; *Corry* v. *Lackey*, 105 Michigan, 363; *Belknap* v. *Stewart*, 38 Nebraska, 304; *Gill* v. *Read*, 5 R. I. 343.

Second. The Trustee contends, however, that since by §§ 18*b* and 59*f* [1] of the Bankruptcy Act, any creditor is entitled to intervene in the bankruptcy proceedings, the Bank should be considered a party thereto. These sections are permissive, not mandatory. They give to a creditor, who fears that he will be prejudiced by an adjudication of bankruptcy, the right to contest the petition. Whether he does so or not, he will be bound, like the rest of the world, by the judgment, so far as it is strictly an adjudication of bankruptcy. But he is under no obligation to intervene, and the existence of the right is not equivalent to actual intervention. Unless he exercises the right to become a party, he remains a stranger to the litigation and, as such, unaffected by the decision of even essential subsidiary issues. *In re McCrum*, 214 Fed. Rep. 207, 213; *Cullinane* v. *Bank*, 123 Iowa, 340, 342. The rule is general that persons who might have

---

[1] Act of July 1, 1898, c. 541, 30 Stat. 544.

Section 18*b* provides: "The bankrupt, or any creditor, may appear and plead to the petition within five days after the return day, or within such further time as the court may allow." (As amended by the Act of February 5, 1903, c. 487, § 6, 32 Stat. 797, 798.)

Section 59*f* provides: "Creditors other than original petitioners may at any time enter their appearance and join in the petition, or file an answer and be heard in opposition to the prayer of the petition."

made themselves parties to a litigation between strangers, but did not, are not bound by the judgment.[1] Compare *Western Union Telegraph Co.* v. *Foster*, 247 U. S. 105, 115. No good reason exists for making an exception in the case of bankruptcy proceedings.

The purpose of Congress in expressly authorizing creditors, as well as the debtor, to answer an involuntary petition in bankruptcy was to guard against an improvident adjudication and to protect those whose peculiar interests might be prejudiced by establishing the status of bankruptcy. See *Blackstone* v. *Everybody's Store*, 207 Fed. Rep. 752, 756; *Jackson* v. *Wauchula Mfg. & Timber Co.*, 230 Fed. Rep. 409, 411. The grant of this right of intervention was harmonized with the general purpose of Congress to secure a prompt adjudication, by requiring that the appearance and answers of creditors be made within five days after the return day on the petition. Had the adjudication been made determinative also of claims of the several creditors against the estate or of claims of the estate against individual creditors, such expedition in proceedings would be impossible, if each of the many widely scattered creditors is to be afforded a fair opportunity to be heard. Furthermore, to require every creditor to acquaint himself with the issues raised in every proceeding in bankruptcy against his debtors, in order to determine whether a decision on any such issue might conceivably affect his interests; and, if so, either to participate in the litigation, or, at his peril, suffer the decision of every question therein litigated to become *res judicata* as against him, would be an intolerable hardship upon creditors. And the resulting volume of litigation would often so delay the adjudication as to defeat the purposes of the Bankruptcy Act.

[1] *Lee* v. *School District*, 149 Iowa, 345, 354; *Weber* v. *Mick*, 131 Ill. 520, 529; *State* v. *Johnson*, 123 Mo. 43, 55; *Hickox* v. *Eastman*, 21 S. D. 591, 595; *Carney* v. *Emmons*, 9 Wis. 114, 117.

The unreasonableness of the rule contended for by the Trustee is well illustrated in cases of alleged fraudulent preference. The claim may be made in respect to any creditor paid off within four months of the filing of an involuntary petition, that he received a fraudulent preference. Is every such former creditor to be deemed an existing creditor within the meaning of §§ 18*b* and 59*f* and a party to the bankruptcy proceeding? Compare *Keppel* v. *Tiffin Savings Bank*, 197 U. S. 356. And shall the decision of the bankruptcy court be binding on all these former creditors in respect to individual claims, although that court could not (without consent) obtain jurisdiction of any creditor who is not a resident of the district in which it sits, *Acme Harvester Co.* v. *Beekman Lumber Co.*, 222 U. S. 300, 311; and would not (prior to the Act of February 5, 1903, c. 487, §§ 8 & 13, 32 Stat. 797, 798, 800) have had jurisdiction, even as against a resident creditor, of a claim to recover a fraudulent preference; such claim being enforceable (without consent) only in courts of general jurisdiction; *Bardes* v. *Hawarden Bank*, 178 U. S. 524; *Wall* v. *Cox*, 181 U. S. 244; *Jaquith* v. *Rowley*, 188 U. S. 620; and, even now, only by plenary suit, *Louisville Trust Co.* v. *Comingor*, 184 U. S. 18; *Babbitt* v. *Dutcher*, 216 U. S. 102, 113.

The decisions of the lower federal courts upon which the state court relied [1] in holding that §§ 18*b* and 59*f* made all creditors parties to the proceeding so as to render

[1] *Cook* v. *Robinson*, 194 Fed. Rep. 785; *In re American Brewing Co.*, 112 Fed. Rep. 752; *Bear* v. *Chase*, 99 Fed. Rep. 920. See also *Lazarus* v. *Eagen*, 206 Fed. Rep. 518. *In re Hecox*, 164 Fed. Rep. 823, also relied upon, is a case of a different character. There, as in *Shawhan* v. *Wherritt*, 7 How, 627, 643, one not actually a party to the proceeding sought to attack the legislative effect of the adjudication—and it was properly held to be conclusive. *Hackney* v. *Hargreaves Bros.* (*Hackney* v. *Raymond Bros. Clarke Co.*), 68 Neb. 633, 639, involved only the admissibility of the schedule of liabilities as evidence tending to prove insolvency.

the adjudication binding on them as to all essential issues, clearly misconceived the intention of Congress. The allegation in the involuntary petition that the Bank was among those who had received preferences, did not impose upon it the duty to appear and answer; and since it did not do so, even a finding to that effect by the bankruptcy court would not have bound it. The Supreme Court of Michigan erred in holding that the adjudication in bankruptcy established conclusively as against the Bank that the debtor was insolvent at the time the payments were made. We have no occasion to consider whether the record introduced was admissible merely as evidence of insolvency.

Reversed.